SUMMER 1976: ONTARIO'S COMMENTS ON SEVERAL CURRENT ECONOMIC AND FISCAL SITUATIONS

Perspectives by The Honourable
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Treasurer of Ontario

The federal **BANK ACT REVIEW**

Ontario feels that Canadian banks have performed well, because of their competence and expertise.

Government policy should focus on the major task of keeping Canada competitive in world markets. Policy should recognize the role our banks play in this process, and in financing industrial and resource projects in the coming decade.

While no basic overhaul of the system is needed, some problems should be tackled. For example, the needs of small business are not being met as well as they could. This calls for innovation and continued investigation by our banks of alternative approaches. Other minor initiatives are also recommended.

In sum, Ontario finds that major government interference with the banking system would not be in the best interests of Canada's economic development at this time.

CORPORATE CONCENTRATION IN CANADA

We find an apparent contradiction in the federal government's twin thrusts, on the one hand toward increased central planning and regulation of private enterprise, and on the other hand toward forcing greater domestic competition in the private sector.

Our stance is that the economic health of Canada dictates action to achieve four urgent priorities: long range price stability, full employment with economic growth, reduced government spending, and restoration of trade balance.

We feel that a healthy and productive industrial structure is the *sine qua non* for these requirements. To be internationally competitive in the present world, Canada must allow her industry and business the efficiencies of size and rationalization. Where decisions must be made between permitting Canada's private sector to remain competitive in the world, and requiring excessive domestic competitive practices, our larger priorities dictate that we support the former.

Federal/Provincial **FISCAL ARRANGEMENTS AND COST-SHARING**

The federal government's June 14th proposal for the re-financing of our health and post-secondary education programs is unsatisfactory to Ontario. The proposal provides for an unfair sharing of the risks associated with future cost developments, and fails to go far enough in giving the provinces the capacity to raise the revenues that they spend.

Ontario proposes that the federal government transfer to the provinces 20 new points of personal income tax in exchange for complete federal withdrawal from hospital insurance, medicare, and post-secondary education. We also insist that there be a replacement for the revenue guarantee beyond 1976, and we have indicated that such a replacement could be integrated into our 20-point proposal to make it attractive to the less wealthy provinces.

ONTARIO RECOMMENDS:

Discussion

1. Provincially regulated financial institutions should continue to play their unique role in Canada's financial marketplace. P2
2. No major changes in the allocation of financial functions should be undertaken at this time. P3
3. The emerging electronic funds transfer system should be supervised by both federal and provincial governments. P3
4. As a priority the review must provide for adequate financial resources to develop and expand our businesses. P3
5. Banks' consumer loan operations (particularly involving credit cards) should be more closely supervised. P4
6. Banks should be permitted to use provincial treasury bills as part of their reserve requirements. P4
7. Formal supervision of foreign banks operating in Canada should be considered. P5

SOME POINTS IN ONTARIO'S POSITION:

1. We are concerned that federal policies could sacrifice the efficiency of our industrial structure in an effort to maintain too high a degree of domestic competition. P8
2. Large companies are often absolutely necessary for the survival and growth of smaller companies. P8
3. We support the industrial distribution which gives the most efficient and internationally competitive industrial structure. P9
4. We understand that productivity is adversely affected by smallness of size and scale. We also realize that R&D and innovative capabilities are a function of size. We want for Ontario and Canada the benefits which follow from industrial rationalization and the economies of scale. P9
5. Tariff policy, not competition policy, is the best way to accomplish competition in our domestic economy. P10
6. Government should encourage strength in Canada's corporate structure, so that it can generate the capital needed for independence in private sector financing. P10

Text of Ontario's presentation to the July 6-7, 1976 meeting of the Ministers of Finance

The Bank Act Review
*A Preliminary Ontario Perspective**

SUMMARY

Ontario believes that the present Canadian banking system is generally serving Canada's needs well and, therefore, that there is no justification for making fundamental changes in our basic financial structure. A modification of the Bank Act could have far reaching effects on the whole complex of institutions composing our financial system.

In recent years, Canadian banks have performed relatively well in a financial atmosphere which has been particularly unstable. They have maintained a universally accepted credit worthiness, where many others abroad have not. Moreover, the success of their performance can be attributed to competence and expertise, since in size the Canadian banks are not large by international standards.

A major upheaval of the business of banking at this time could create a degree of uncertainty in the business community which could retard economic growth. At the present time, government policy should be focused on keeping Canada competitive in world markets, and should recognize the role that our banks play in this process. Similarly, it is important to recognize the essential role that banks must play in financing large industrial and resource projects of the coming decade. Sound large-scale financial institutions are vital for Canada's industrial development.

Competition in Canada's capital markets is ensured because banks face vigorous competition in providing service from other domestic and foreign financial institutions. It is noteworthy that, over the past decade, bank assets have grown more slowly than the assets of the major near-banks, trust companies and credit unions. In spite of this competitive environment, the needs of some sectors, like small businesses, are not being met as well as they might and, thus, the banks must continue to investigate alternative approaches and seek innovative solutions.

Further government involvement or interference with the banking system would not be in the best interests of Canada's economic development at this time. Considering the need to ensure the continued health of our financial system and recognizing the need to meet demands of the future, however, the following specific suggestions are put forward:

1. **Provincially regulated financial institutions should continue to play their unique role.**
2. **No major reallocation of financial functions should be undertaken for at least five years.**
3. **The emerging electronics payments system must be closely supervised by both the federal and provincial governments.**
4. **The role of banks in providing capital to develop and expand Canadian businesses should be a priority.**
5. **Bank consumer credit operations must be more closely supervised to ensure greater protection to customers and the Canadian economy.**
6. **Banks should be permitted to use provincial treasury bills as part of their reserve requirements.**
7. **Formal supervision of foreign banks operating in Canada should be considered with a view to ensuring the ability of Canadian banks to compete abroad.**

THE CONTEXT

The Bank Act is presently being reviewed by the federal government in preparation for the decennial revision in 1977. This is an event of major significance. A modification of this Legislation could affect the whole complex of institutions composing the financial system which is the very heart of our economy. The Government of Ontario has taken a great deal of interest in the variety of proposals for revisions of this Legislation and has viewed with concern suggestions that a major overhaul be undertaken. Below, Ontario sets forth for consideration its own

**Submitted to the federal government in May, 1976.*

general thoughts and some specific suggestions on means to ensure the continued health of our financial system.

THE ONTARIO VIEW

At the outset, it should be emphasized that Ontario does not favour massive restructuring of the banking industry or increased government involvement in the business of banking. The existing banking system is serving Canada's needs fairly well and, with the important economic issues currently facing the country, now is not the time to experiment with Canada's basic financial structure. Within this structure, however, some improvements and additional safeguards are possible.

The Canadian banking system ranks among the strongest in the world. Canadians have not had to suffer bank failures such as have occurred in Europe and the United States in recent years. Canadian banks have been able to maintain their universally accepted credit worthiness in the face of the dramatic contractions in the Euro-dollar market which cast a shadow over many of the world's largest financial institutions. The size of Canadian banks has also made it possible for this country to finance massive resource and industrial projects essential to our economic growth.

Ontario is particularly concerned about the degree of regulation and interference in the economy initiated or proposed by the federal government in recent years. This has created a degree of uncertainty in the business community which could retard future economic development. **Proposals for a major restructuring of the financial system now could seriously compound this uncertainty at a time when it is important to focus on the national priorities of long term economic recovery, international competitiveness and a successful completion of the Anti-Inflation Program.**

Contrary to popular opinion, Canadian banks are not giants by international standards. The largest Canadian chartered bank ranks 15th in the western world (measured by size of deposits) and only three Canadian banks are among the top fifty.*

A fundamental problem facing Canada as a trading nation is improving the productivity performance and competitive position of our industries. A dynamic financial system is a prerequisite to providing the industrial expansion and rationalization which will keep Canada competitive in world markets. The specialized expertise which our banks supply to Canadian exporters is possible only because our banks are international organizations with a thorough knowledge of overseas opportunities. **Ontario's industrial base is heavily dependent on the export of manufactured goods and a strong banking system will be essential for maintaining a strong performance in this sector.**

Size and scale are also important considerations in the ability of banks to meet future domestic capital market requirements. Over the next decade, we expect to see a number of major industrial and resource projects undertaken in this country. The scale of financial resources required will involve a large and efficient financial structure. The public sector will play an important role in some of these, but it is increasingly clear that **if the growth of government's spending and its demands on capital markets is to be contained, funds will have to come from private enterprise.** Sound, large scale financial institutions are therefore vital for Canada's industrial development.

The size of individual Canadian chartered banks has not necessarily lessened competition in the financial sector. Banks face vigorous competition from regional banks, foreign banks in Canada and other near-bank institutions such as credit unions and trust, insurance, leasing and acceptance companies. In fact, since the last Bank Act revision in 1967, bank assets have grown more slowly than those of their nearest rivals — the trust companies and credit unions.

Ontario is concerned by increasing suggestions that the Bank Act be changed to permit provinces to play a broader role in owning and controlling chartered banks. There is no legitimate reason for government involvement in an area where private enterprise has already demonstrated its ability to do a good job. **Such a blending of the private and public sectors in a single financial institution could result in a dangerous concentration of power.**

While an overhaul of the banking system is neither necessary nor warranted at this time, Ontario does have a number of suggestions which should be considered within the context of any revision of the Bank Act.

SPECIFIC CONCERNS

Provincial Regulation

Vigorous competition in the financial sector has often come from non-bank financial institutions such as trust companies, credit unions and life insurance companies. Although often small in absolute and relative terms, these institutions have grown over the years by providing the public with specialized and efficient services. Indeed, much of the innovation in Canadian

**American Banker*, July 31, 1975, p. 62.

financial services has stemmed from these institutions. Provincial regulation of a number of these financial institutions has contributed to their uniqueness and innovation.

The Canadian economy is characterized by regional diversity. Provincial regulation of a number of financial institutions has provided a regional flavour and ensured a capability to adapt to local needs. In Ontario, for example, the application of Section 90 of the Ontario Loan and Trust Corporations Act has reflected a high priority in the province for housing.

> *Recommendation: Provincially regulated financial institutions should continue to play their unique role in Canada's financial marketplace.*

Financial Functions

The existing structure of Canada's financial markets is characterized by a fairly clear demarcation and allocation of financial services among competing types of institutions. For example, while certain non-banks are generally much smaller than the large chartered banks, this size disadvantage is partially offset by certain prerogatives of the near-banks which are not available to the chartered banks. In the past competition in financial markets has been effectively maintained by this method of ensuring diversity. At the same time the banks have been able to direct financial resources to these other markets by engaging indirectly through subsidiary investments.

While a detailed analysis of different financial services might be required, it does not appear that a major shift in the allocation of services such as trust, factoring and leasing functions would be desirable at this time.

> *Recommendation: No major changes in the allocation of financial functions should be undertaken at this time.*

The Payment System

Over the next decade, our financial system will become increasingly dependent on electronic funds transfers, moving away from the present paper based payments system. This trend will bring with it a host of economic, legal and social problems and issues bearing upon both federal and provincial jurisdictions.

Not the least of these problems will be the question of access to these new systems as they develop. It will be especially important to ensure that all financial institutions have access, and that evolving technology be made available to all users. The federal government's *Statement of Government Policy Concerning Computer/Communications and the Payments System* reflected a desire to forestall the possibility of a few large firms gaining monopoly control over the evolving EFTS by virtue of their early large scale entry into this field.

However, because of their jurisdiction over many financial institutions which will be using the EFTS and the potential impact of the EFTS on a wide range of provincial statutes, it is imperative that provincial governments play an important role in the development and implementation of policy in this area. In particular, the provinces should be actively involved in two of the national study groups now being established: The Credit/Payment Study Group and the group examining legal and consumer issues arising from the use of electronic technology in the payments system.

> *Recommendation: The emerging Electronic Funds Transfer System (EFTS) should be closely supervised by both the federal and provincial governments.*

Financing Canadian Business

There is a pressing need for the development of an enlarged venture capital industry in Canada capable not only of supplying equity funds but also of providing financial management expertise, technical assistance and other services needed by small businesses. The role of the banking community in overcoming this problem should be expanded.

Canada's banking industry in future must be sensitive to the priority of improving our productivity performance and encouraging the growth of Canadian enterprise. In the past Canada's banking legislation has been primarily concerned with bank liquidity and security. While this is a legitimate and primary concern of the Bank Act, these needs should be better balanced against the size and role of chartered banks in Canada's economic environment. Specifically, the banks should be encouraged to make a greater contribution in the provision of venture capital and of capital for Canadian businesses generally.

A second aspect of this issue concerns the effectiveness of financial assistance provided by Canadian lending institutions under the federal Small Business Loans Act. The incentive provided by the legislation could be expanded by raising the limitations on lending amounts and rates.

> *Recommendation: A priority of the Bank Act review must be the provision of adequate financial resources to developing and expanding Canadian businesses.*

Bank Consumer Credit

Since the last Bank Act revision the banking industry has become a major source of consumer credit. This has led to some concern about a number of potential problems such as:

- inflationary impact of easy access to consumer loans;
- encouragement of over-extension of household finances;
- discrimination in the accessibility of credit, particularly in credit card operations.

A significant factor contributing to inflation in Canada in recent years has been a dramatic increase in expectations for immediate consumption and a rapidly rising standard of living. This, in part, has been facilitated and encouraged by an overly aggressive approach by the banking industry to the marketing of consumer credit. Young families, encouraged to accumulate household assets on the basis of easy credit, perhaps too quickly translate this into expectations and income demands which may fuel the wage-price spiral.

Another aspect of the current bias towards consumer credit concerns the implications for the future performance of the Canadian economy. With the pressing needs for capital expansion in energy, manufacturing and resources, Canada can ill-afford to encourage an excessive allocation of scarce capital resources to consumption.

In a similar vein, the ease of access and marketing enthusiasm associated with consumer credit may be leading to a dangerous over-extension by some Canadian families. The expansion of credit availability through credit cards in recent years is particularly worrisome in this respect. While still a small part of bank personal loan outstandings, the rapid growth of credit card outstandings in the past few years suggests that this area will be one of growing concern. It is an area, furthermore, about which too little is known.

Finally, there are special concerns about the protection of the interests of credit card users in a market in which regulation is largely absent. Banks clearly have both the right and the obligation to carefully screen all applications for credit cards. There are, however, indications that some individuals and groups have been arbitrarily denied access to this important source of credit. For example, women often face discrimination from lenders. Although the Ontario Government has moved to prevent provincially regulated financial institutions from following this practice, federal legislation is necessary to encompass the chartered banks.

The credit card billing procedure used by banks is also in need of some government supervision. Banks must be made to assume greater responsibility both for their own errors in billing and for the business practices of firms using their credit card systems.

> *Recommendation: Banks' consumer loan operations—particularly those involving the use of credit cards—should be more closely supervised to afford greater protection for the rights and interest of bank customers and to serve the needs of the economy as a whole.*

Provincial Treasury Bills

In recent years, over 95 per cent of all Federal treasury bills have been held by the Bank of Canada and by the chartered banks, the latter in order to satisfy their secondary reserve requirements. As a consequence, the competitiveness of the short term debt market has been severely reduced and the federal government has been able to impose what is, in effect, a monopolistic tax on chartered banks. Ontario believes that the inclusion in secondary reserves of provincial bills and day loans secured by provincial bills would encourage fairer treatment of all market participants, increase competition at the short end of Canadian markets, improve the efficiency of the Bank of Canada's open market operations, and increase the financing options open to both governments and chartered banks.

The banking system would receive more equitable treatment since banks would be able to bid for reserves in a competitive market. Substitutability

between the various instruments that comprise the short term debt market would increase thus permitting the effects of monetary policy to be spread more rapidly and over a wider range of instruments. Because provincial and corporate debt are reasonably close substitutes, a more integrated market would also result.

Recommendation:	*Banks should be permitted to use Provincial Treasury Bills and day loans backed by Provincial Treasury Bills to satisfy secondary reserve requirements.*

Foreign Banks in Canada

In recent years the lending operations of foreign banks in Canada have grown at an accelerating pace. They compete with Canadian financial intermediaries in providing a number of services, but they are generally not subject to the same kinds of supervision which Canadian banks and near-banks face. Relatively little is known about the size and nature of their operations, but it is generally felt that they are a significant force in certain financial markets. It would be useful to have some kind of supervision to ensure that they were as consistent as possible with the goals of Canadian monetary policy.

Furthermore, it has been argued that formal recognition of foreign banks operating in Canada would be useful in obtaining reciprocity for Canadian banks operating in other countries. Our major concern is that Canadian banks are able to help Canadian industry to compete abroad and to ensure our exporters fullest access to world markets.

Recommendation:	*Formal supervision of foreign banks operating in Canada should be considered.*

This section is from the text of the Submission by The Honourable W. Darcy McKeough to the Royal Commission on Corporate Concentration—June, 1976

INTRODUCTION

The basic objective of the Province of Ontario is to continue to expand job opportunities and per capita income growth well into the future. In a large part, our ability to do this will depend on maintaining a healthy and productive industrial structure which I assume is also the major concern of the Commission.

I don't think it's exaggerating to say that Canadian economic and social development is at a crossroads. I went into some detail on this in my recent Budget Statement where I called for the development of a national economic policy for Canada.[1] Here, I would briefly point out that the country is involved in major reviews of energy, transportation and population policies. The GATT negotiations now getting underway in Geneva are going to force us to take a pretty close look at our future trade and industrial strategy over the next few years; in particular, the question of productivity of our industries. A review of the Bank Act is underway and we expect that the issue of competition policy will come to the fore again in the near future, possibly as a result of the deliberations of your Commission. Finally, in my 1976 Budget, I pointed out that we see a number of fundamental problems developing in Canadian-U.S. auto trade which must be dealt with in the near future.[2]

While all of these issues are concerned with the longer term economic future of the country, two very important short run economic issues are also commanding a great deal of attention. They will also have important long run economic significance.

I refer here to the Anti-Inflation Program initiated by the federal government and strongly supported and complemented by Ontario. Second, I have in mind the attempts being made by all levels of government, and in particular by the Government of Ontario, to drastically reduce the rate of government spending growth. **Success or not in these two areas is going to have a great deal to do with our future capacity for healthy economic growth and job creation.**

There is one common thread which runs through all of these issues. They all call into question the role of private business in the future growth and development of our economy. Most of these issues potentially involve increased government regulation, direction and control of economic resources. And they all create an added degree of uncertainty for private business with respect to its future structure and operation in our economy. **This uncertainty makes investment decisions riskier and thus imposes additional real costs—costs which ultimately will have to be borne by the consumer.**

Before zeroing in on the issue of corporate structure and concentration, I would like to make an observation on what I perceive to be a contradiction in the broad thrust of economic policy as practiced by our federal government. Without going into details, the drift of federal economic policy appears to be towards more central planning and regulation of private enterprise. The most spectacular demonstration of this, of course, is the Anti-Inflation Program. Yet, while government gets bigger and more powerful, another thrust of economic policy has been to promote increased competition in the private sector.

While I can accept the need for more government presence in certain aspects of economic activity, at the same time I also accept the fact that in many sectors businesses are going to be larger and more concentrated in the future. *And I do not think that we should necessarily resist this trend with outdated notions of competition between a large number of small firms.* The fact is that large, world-scale plants are often necessary to reap economies of scale and to compete in international markets. And in the domestic market, bigness and competition are not always incompatible. Accordingly, I am concerned about apparent federal thinking on competition policy.

I believe that any specific concerns about industrial concentration should be related to national economic objectives. While, perhaps, it is beyond the Commission's terms of reference to consider what general economic objectives this country should adopt, I would like to suggest some which I think are

[1]The Honourable W. Darcy McKeough, "A National Economic Policy for Canada", Budget Statement, *Ontario Budget, 1976*.

[2]The Honourable W. Darcy McKeough, "Performance Under the Auto Pact: An Ontario Perspective", Budget Paper F, *Ontario Budget 1976*.

"motherhoodish" enough to be more or less beyond controversy. At the same time, I will briefly relate my views concerning corporate concentration to these objectives. The four objectives which I would like to discuss relate to price stability, economic growth, government spending and international trade.

The first objective is long run price stability in Canada. Jumping ahead a few years and assuming some degree of success with the Anti-Inflation Program, one of the major contributors to price stability will be productivity improvements in the private sector. Large plant and firm size is often necessary for the full utilization of technological and managerial economies of scale. As a result, large firms are better able to keep unit costs down. The image of many small, highly competitive firms bidding prices down can be fallacious in certain circumstances when massive marketing and research expenditures may be necessary to reduce unit costs.

The second objective is that of full employment and a healthy rate of economic growth. Ultimately, real economic growth and the creation of more jobs is fueled by new investment in the private sector. Canadian firms can attract needed capital *only* if they are earning a healthy return on investment. Depending on the markets in which they operate, this often means that they must be large in order to take full advantage of the best production processes and to effectively compete in international markets. This will be particularly important if we are to provide enough jobs to meet the needs of Canada's fast growing labour force.

The third objective concerns the need to reduce the rate of government spending increases. Successful reduction in government spending growth will result in a lower relative level of taxation, but it will also place significant responsibilities on the private sector, which will have to pick up a greater share of programs in areas such as research and development, pollution control, employee benefits and the funding of new and risky business development. (Perhaps this is the other side of the coin that people do not think about when they argue for lower government spending and hence lower taxes.) It will be the large firms which are the most capable of assuming these expenditures. If they do not, the onus will be back on government.

The fourth economic objective concerns Canada's trade balance. The development of a productive industrial structure capable of competing successfully in international markets is the best assurance that Canada's international current account deficit will, in future, be reduced. And here we have some grave concerns about Canada's relative productivity performance and competitiveness, as I pointed out in my latest Budget.

That concludes the introductory portion of my remarks. I would now like to go into more detail concerning Ontario's views on corporate concentration. To some extent, I will further elaborate on the themes which I have outlined above, and I will also introduce a number of additional points.

INDUSTRIAL POLICY FOR CANADA

Priorities

To begin, I would like to suggest that government policies with respect to industrial concentration must be formulated within the context of a comprehensive industrial policy for Canada. Initiatives in the area of corporate concentration are bound to have many far-reaching effects. They will, in all likelihood, influence employment, resource development, foreign trade and investment, research and development and the regional development of Canada. It is important, therefore, that these relationships are borne in mind when determining the role which future competition and concentration policy is expected to play in an industrial strategy for Canada.

In Ontario we are concerned that the federal government may ultimately adopt a course of action which unreasonably emphasizes competition as a national objective, thereby closing off certain industrial strategy options before they are properly considered. **The priority which the federal government has in the past assigned to competition is, in our view, misplaced.** This was particularly true of the original set of amendments to the Combines Investigation Act, Bill C-256, which was introduced in 1971. Although the Bill was subsequently withdrawn, the possibility that some of its provisions may be reintroduced in the upcoming "Stage II" Legislation raises the concern in our minds that the development of an efficient industrial structure may be sacrificed in an attempt to maintain a high degree of competition at home.

Large vs. Small

I am worried that excessive concern with domestic competition will cause us to lose sight of an important relationship between large and small firms. What I had in mind here is that large industrial companies typically purchase many of their supplies from smaller firms. The automobile, steel and shipbuilding industries, to cite but three examples, provide important

markets for many small Ontario firms. **Small companies have a vital stake in the continued growth of their large customers — growth which can continue only if we pursue an industrial policy based on Canada's special needs and priorities.**

We also recognize that small firms, compared to the large ones, are handicapped in their competitive strength in areas of management, credit availability, technological know-how, and access to the more distant markets. The provincial government in Ontario has therefore operated industrial and trade support programs specifically designed to help small companies so that they grow and prosper. Also we have recently reduced the Ontario preferential tax rate for small businesses from the previous 12 per cent to 9 per cent.

Regional Distribution

There is another dimension to the issue of industrial policy. It concerns the regional distribution of industrial production. In the context of the national debate over oil pricing, once again we have heard complaints about the concentration of industrial activity in central Canada. We are concerned that this could lead to an over-emphasis in the future on regional problems at the expense of important national economic priorities of efficiency and competitiveness.

Ontario has always supported measures to encourage a broader distribution of economic growth, but I think this must be placed clearly in a national context. Basically we face, as we always have, three alternatives.

First, we can virtually eliminate all tariffs. In some cases this will lead to cheaper imported goods flowing to all Canadian regions thus benefitting consumers, but at a cost of jobs, incomes and long term security.

Second, we can insist on more regional diversification of employment. This increases local jobs and incomes, but at a cost of inefficiency, higher prices for consumers and higher taxes to support certain industries.

The third alternative is to promote the industrial structure which is most efficient and internationally competitive even if this means continued concentration of some industries in central Canada. I think it is clear that this option is the only viable one in terms of Canada's long term economic development. If we are going to follow this course, I am prepared to support the principle of using tariff policy as an instrument for encouraging international competitiveness. I will expand on this shortly when I deal with the issue of productivity.

The whole issue of industrial strategy is a difficult one and I do not pretend to have all of the answers. But what we are saying is — **put the issues of competition and regional growth in the context of broader economic priorities.**

PRODUCTIVITY

While no one can specify now what the exact nature of future industrial strategy for Canada should be, I think we can agree that central to any strategy must be a heavy emphasis on improving the productivity of our economy. Judged by international standards, many of our firms are of sub-optimal size. For example, the size of the average industrial plant in this country is only about half that of its counterparts in the United States and Germany. This means that the scale of output in Canada is severely restricted, leading to higher costs and prices and making it difficult to increase productivity. I am sure that this is one reason why our productivity *dropped* by almost 2.5 per cent last year.

In my Budget Statement I drew attention to Canada's deteriorating trade balance. Part of this, no doubt, reflects the relative economic performance between Canada and the United States in 1975, but I think there are more fundamental factors involved as well. While we have moved to wage and salary parity with the U.S. in a number of industries, productivity has not kept pace. **Part of the cause of this productivity gap, it seems to me, lies in the smaller size and scale of Canadian business operations.**

Looking to the future, we view this as a very serious situation. Small plant size not only makes our goods more expensive but also means that many firms earn an inadequate rate of profit. New investment is discouraged and this, of course, hurts employment and economic growth. Sadly, this trend is still continuing today. Industrial plants now being constructed abroad to supply world markets are often much larger than those which exist in Canada. Only the very largest Canadian firms can keep up. For example, to take full advantage of technological economies of scale, an oil refinery must have a capacity of around 125,000 barrels per day, a copper smelter and refinery complex must produce about 100,000 tons per year and a steel plant about 5 million tons per year.

If we are to improve our productivity, a number of alternatives will have to be considered, but I do not think there is any doubt that consideration

must be given to the benefits which can be achieved through industrial rationalization. All too often, we lose sight of the fact that the openness of our economy means that foreign suppliers, particularly those next door to us in the United States, provide vigorous competition in the Canadian market place. **In this context, Canadian tariff policy, not competition policy, should be viewed as the ultimate weapon to ensure that competition prevails in the domestic economy.** We feel, therefore, that the federal government should refrain from promoting domestic competition as a strong economic objective in itself and concentrate instead on developing coordinated policy which will provide the flexibility necessary to permit efficient restructuring of the Canadian economy.

INTERNATIONAL COMPETITION

I would like to switch the focus slightly to the changing international competitive environment. Canadian firms sell a large proportion of their output abroad and, at the same time, imports account for a substantial share of our domestic market. In other words, Canada is a major trading nation.

With trade liberalization, which may accelerate as a result of the GATT negotiations now underway in Geneva, it has become impossible for our firms to insulate themselves from international conditions. Many important industries are dominated by world-scale producers (whose goods are often promoted abroad by large state or private trading companies) located in the United States, the European Community and Japan. **If Canadian companies are to be able to compete effectively with these industrial giants, they must be allowed to take maximum advantage of technological and administrative economies of scale.**

Failure to do so will result in reduced foreign sales and increased penetration of foreign goods and services into our markets resulting in loss of employment and aggravated balance of payments difficulties.

I think it is true to say that our growing trade deficit in secondary manufactured products may be a reflection of Canada's relatively weak and vulnerable industrial structure. There are, of course, many reasons for this country's large deficit in manufactured products, such as our proximity to large U.S. producers and tariff and tax policies both in the United States and Canada. But it is also clear that a large part of the explanation lies in the absence of a stronger and more productive industrial structure in Canada.

INNOVATION

I would like to move on to an area that relates closely to both international trade and productivity — that is, innovation. I think that part of our problem lies in our failure to develop the innovative capacity necessary to compete more successfully in world markets. This problem, I might point out, has been recognized by the Senate Special Committee on Science Policy, chaired by the Honourable Maurice Lamontagne. In one of its reports,[3] the Committee specifically addressed itself to the connection between Canada's competition policy and our inability to develop a desirable level of research and development activity.

To underline our apprehension concerning this problem in Ontario, I will briefly quote from the document:

> *"A serious deficiency of many Canadian manufacturing industries is their fragmentation into small but unspecialized firms, which cater mainly to the domestic market. Failure to specialize weakens their ability to innovate or to compete in export markets. While this fragmentation has other causes, it may be perpetuated by Canadian competition policy . . .*
>
> *"The Committee has received many complaints from industry about the interpretation and administration of the Canadian Combines Investigation Act. Companies have contended that many industries are too fragmented to develop an innovative capacity or to afford even a minimum critical mass of R & D activities. It has also been argued that the interpretation of Canadian legislation rests on the concept of 'free competition' and thus often prevents mergers and specialization specifically designed to meet the problem of scale."*

All I can say in commenting on this is that I could not agree more.

CAPITAL

I would like to turn to the question of the availability of capital to industry over the next decade.

We are all well aware of the looming problem, if it is not already with us, of generating enough capital to finance needed expansion of the Canadian economy, particularly in the energy-related sector. This is a problem that is directly affecting both

[3]Science Policy for Canada, Volume 2, 1972.

governments and the private sector. As Ontario Treasurer I have had to deal with the problem in a very immediate sense, and you may be aware of the cutback in Ontario Hydro's expansion program as a result of necessary financial constraints.

I am concerned that in future only the largest companies will be capable of generating the required funds internally or through external borrowing to finance needed expansion. The Petrosar project in Sarnia, for example, will cost almost half a billion dollars and has required a consortium of several of Canada's largest chemical producers. This problem is likely to become even more acute in future as minimum plant size requirements grow and construction costs increase. Government, of course, will step in on occasions as a financing partner as, for example, we have in the Syncrude project. **However, we cannot and should not depend exclusively on this route to meet our future investment requirements.** Rather, we should be encouraging a greater degree of industrial rationalization so that our corporate structure will be strong enough independently to meet its financing requirements.

CORPORATE DIVERSIFICATION

I would like to turn briefly to the issue of corporate diversification. As is the case abroad, many of Canada's major firms produce and sell a wide range of products and services. While the economies of scale at the corporate level are not always as easily identified and quantified as those at the individual plant level, they are nonetheless significant.

A major portion of the output of Canadian firms consists of by-products or joint-products. Similarly, many products with quite different end uses may be made by one company on the same plant site, often with the same raw materials or related technology. In producing a diversity of products at a single plant site, the company and ultimately the consumer benefits from efficiencies which result from spreading overheads as widely as possible. **Management, engineering and marketing techniques are all examples of skills which, because of the time and expense required for their effective development, can only be supported by a large corporation.**

While on the issue of diversification, I might make one final point concerning takeovers. The public image of corporate diversification and takeovers is one of financial manipulation. In fact, some companies involved may often be revitalized by this process through the injection of new management and capital.

CORPORATE POWER

I would like to conclude this brief with some general observations on the question of corporate power itself. I would like to suggest that any evaluation of corporate power must always be judged within the context of power concentrations in other areas of the economy, most notably government and labour. Canadian corporations do not operate in a vacuum— they are in constant contact (and indeed sometimes conflict) with the large and growing forces of government and labour. The corporation must increasingly deal with other bodies as well, such as community, consumer and environmental groups. If viewed in isolation, corporate power may at first seem boundless and invincible, but this is hardly the case.

Over the past decade, we have imposed responsibility for a great many social and economic priorities on our corporations. I have in mind tax reform, consumer protection, foreign investment legislation, environmental protection and bilingualism and, just recently, the Anti-Inflation Program. There have been sound reasons for implementing these policies, but, at the same time, we still expect corporations to provide expanding employment and economic growth which is the foundation of our social well being. Accordingly, I think we have to pay close attention to international economic realities and ensure that the policies which govern corporate structure and concentration are consistent with the objectives of international competitiveness and productivity. **In order to meet these objectives, I think we are going to have to come to the realization that, to some degree, corporations are going to have to be powerful and they are going to have to be large.**

This section is from the text of the statement by The Honourable W. Darcy McKeough at the meeting of the Ministers of Finance—July, 1976

PROVINCIAL PRINCIPLES

On June 14, the Prime Minister of Canada presented the provinces with a new proposal for the joint financing of our health and post-secondary programs. His proposal is an extremely important one—it involves a major change in the existing arrangements, and affects over $10 billion in combined federal and provincial spending.

The Prime Minister began his statement by listing the five principles that lie at the core of his approach to financial reform. Ontario is in broad agreement with these principles, as we indicated at the Meeting of First Ministers on the 14th of June. However, now that we have been given more details, it is clear that the method of implementation is unsatisfactory. Before analyzing the federal proposal, I would like to set out what I perceive to be the five principles that are held in common by all the provincial governments.

First, the provinces believe that there must be an equitable division of the responsibility for cost control. Throughout the discussions of the last five years, the provinces have never disputed the need for greater program economies. What they *have* disputed are federal attempts to shift an undue burden of responsibility onto provincial shoulders. The various federal proposals of the past have not fairly recognized the steps that provinces have already taken to contain cost pressures, nor have they realistically appraised provincial abilities to contain costs in the future. A realistic division of the responsibility for cost control means, among other things, that the federal government must face up to the fact that it, itself, was a contributor to the present cost problem, insofar as it forced the provinces to join a universal Medicare program, and insofar as it was unable to control inflationary pressures in the economy generally.

Second, the provinces believe that GNP is a completely inappropriate escalator. The use of federal fiscal leverage to force program economies has never really been disputed in principle; what is at issue is how this is done. The federal view is that cost control should be forced upon the provinces by reducing the growth of federal shared-cost contributions to the rate of growth of the economy as a whole. This "GNP principle" has permeated federal thinking for several years now—it was part of the Faulkner education plan rejected by the provinces in 1973; it was part of the Lalonde health plan rejected by the provinces in 1974; and it is implicit in the equalization and shared-cost ceilings that have recently been imposed to the detriment of all provincial governments.

The provinces have all along insisted that it is unfair to tie transfers to GNP. GNP growth does not match the expected growth of program costs, even under maximum assumptions about provincial cost control. Moreover, tying federal funding to GNP would mean that transfers to provinces would decline as a percentage of the federal budget. The corollary is that the federal government would reap huge fiscal dividends. From the provincial point of view—and I think I can speak for all my colleagues—the minimum that we can accept is a constant share of the federal budget, that is, a growth in transfers equivalent to the growth in federal revenues.

Third, the provinces believe that any financial "benefit-of-the-doubt" should rest with them, not with the federal government. Considering the great and historical fiscal imbalance in this country between the federal government on the one hand and the provinces and municipalities on the other, and considering the funds that are being "recaptured" from the provinces by unilaterally changing the Revenue Guarantee and introducing transfer ceilings, and considering the untimely death proposed for the Guarantee, and considering the massive revenue losses imposed on the provinces by the indexing of the personal income tax—considering all these things, it seems to us obvious that any financial "benefit-of-the-doubt" should lie in the provincial favour. In the context of our recent experience it is particularly annoying that the federal government should seek not only to extricate itself from all future risks, but also to secure yet another long-run revenue advantage at provincial expense.

Fourth, the provinces believe that all matters before us should be treated as a package, not

as separable issues. The federal approach has been to talk about re-financing Hospital Insurance and Medicare, while continuing to ignore the 20 per cent of health spending which is not presently cost-shared. This is not only irrational, it is an invitation to future confusions and frustrations. The federal government has also insisted that equalization and the Revenue Guarantee be treated separately from the shared-cost programs, failing to recognize the crucial trade-offs that must necessarily be a part of any eventual agreement. The provinces are concerned that the future arrangements be fair, and the only way to ascertain and ensure this is to look at all fiscal matters as interrelated—which they most assuredly are. Our meeting today is the first chance that Ministers have had to discuss the overall picture. I welcome the opportunity.

Finally, the provinces insist that our new fiscal arrangements be simple to both administer and understand. Implicit in this principle is a disentanglement of responsibilities and greater flexibility for the provinces to follow their own priorities.

The principles that I have taken the liberty of summarizing are the criteria by which we must judge the new federal initiative. Keeping them in mind, let me now consider the details of the proposal.

ANALYSIS OF THE FEDERAL PROPOSAL

PERHAPS THE MOST STRIKING OBSERVATION THAT ONE CAN MAKE IS THAT THE FEDERAL GOVERNMENT HAS PROGRESSIVELY DEVALUED ITS OFFER OVER THE LAST TEN YEARS. This can be seen by setting aside various complexities and concentrating solely on the income tax room that has been offered. In view of the fact that the provinces have repeatedly stressed the desirability of personal income tax points as a form of compensation, this is a perfectly legitimate way of comparing the various federal initiatives.

In 1965, the Government of Canada enacted The Established Programs (Interim Arrangements) Act. This advanced piece of legislation permitted a type of conditional opting out, and awarded *16* points of personal income tax in lieu of shared-cost payments for Hospital Insurance. Contrary to provincial hopes, this offer never became open-ended; it was withdrawn in 1969, by which time only Quebec had accepted.

In the spring of 1973, the so-called Lalonde-Turner proposal was presented to the provinces. This financing package included only *6* points of personal income tax for *both* Hospital Insurance and Medicare.

The latest federal proposal further reduces the number of tax points offered. The apparent "outside limit" is now down to 3.143 new tax points, and this is for *three* programs: Hospital Insurance, Medicare *and* post-secondary education.

This short history explains the widespread provincial frustration that is all too apparent in the current negotiations. **Regardless of the total dollars that may or may not be on the table, the record shows that the federal government has consistently backpedalled on the issue of income tax room.** The facts of the matter just don't reconcile with the Prime Minister's recent assertion that the government that does the spending should also do the taxing.

A SECOND CRUCIAL OBSERVATION IS THAT THE CURRENT PROPOSAL IS NOT REALISTIC OR FAIR. The proposal will reduce the growth of total federal contributions to approximately the rate of growth of GNP. The following table indicates that for the three programs in question, Ontario's expenditures have traditionally grown in excess of GNP.

	1970-71	1976-77	Growth Over Six Years
	($ million)		(%)
Ontario shareable costs—3 programs	1,829	4,075	123
G.N.P.	85,685	176,500	106

Looking to the future, we cannot realistically expect to bring our program growth down to the extremely low GNP target. In order to appreciate this, one must consider the sources of cost pressure, and also the restraint measures that have been taken, and might reasonably be expected to be taken, in the years ahead.

Health Care

Insofar as health care is concerned, the Government of Ontario has consistently argued that escalating costs are due to three things: **high and growing utilization rates, wage and salary inflation, and a cost-sharing structure that inhibits the development of low-cost alternatives to hospitalization.**

The utilization rate is a serious problem—in Ontario, medical visits *per person* are 20 per cent higher today than they were four years ago, and the rate of hospital admissions is now growing at double the rate of population increase. This high and growing

utilization rate is explained by two things. The first is universal Medicare, a program which has a built-in "price incentive" for people to seek frequent medical attention. The second is the high doctor-to-population ratio that has been allowed to develop in this country. The record shows that the Government of Ontario has taken major and often unpopular steps to reduce health care costs; in fact, **we have succeeded in moving our per capita costs down to the national average.** This is no mean accomplishment when it is remembered that growing utilization of the delivery system tends to offset efforts directed at program economies.

Wage and salary inflation in the public sector has also been a major reason for cost pressure. Labour costs account for about 70 per cent of hospital operating costs, and settlements are now running in the neighbourhood of 15 per cent. A "catch-up" in the relative incomes of hospital workers was clearly warranted; and **the Government of Ontario is not willing to accept that the consequence of shared-cost reform be a return to an inferior income status for these individuals.** This is not to say that Ontario has been, or will be "indulgent." Our record is exemplified by the agreements we have reached on fee schedules with the cooperation of the Ontario Medical Association.

Third, cost pressures are created by the federal government's failure to share on lower-cost alternatives. **The fact that the federal proposal does not explicitly address this problem means that obstacles to cost effectiveness and priority-setting will likely continue for some time.**

Education

Turning to post-secondary education, the difficulties are again with utilization and inflation. Changing economic and social circumstances are responsible for the continued growth in our post-secondary clientele, and especially for the increasing participation by the adult population. **Again, these are forces over which the provinces have little or no control.**

I have tried to demonstrate that GNP growth is an unrealistic target. It is *so* low that the provinces could not reasonably be expected to meet it, given the steps that have already been taken, and given that the real sources of cost pressure are largely beyond their reach. But GNP growth is unfair for yet another reason. Even if, by some stretch of the imagination, the wealthy provinces could get by with GNP escalation, there would still be a problem for the poorer provinces. Like Ontario, these provinces have experienced cost growth higher than GNP, but their problem of cost control is further compounded by the fact that they are in the middle of a service and wage-level "catch-up." Compared to these irresistible catch-up pressures, the bonus to some provinces through the proposed five-year per capita levelling must surely seem a small consolation.

A THIRD OBSERVATION CONCERNS THE CHOICE OF A BASE YEAR. Figures presented by federal officials compare how much provinces would receive under the new proposal with how much they would receive under the current arrangements. **The subterfuge here is that the current arrangements have been projected, not on the basis of real costs, but on the basis of the existing maximum growth allowed by federal ceilings.** The financial comparisons are therefore misleading, and can only be described as a form of economic gerrymandering.

A FINAL OBSERVATION THAT I WOULD LIKE TO MAKE AT THIS TIME IS THAT THE FEDERAL GOVERNMENT IS APPARENTLY STILL WEDDED TO THE IDEA OF A TAX "MIX." It has suggested that if more than a third of the replacement funding is to be in the form of tax room, the package will have to contain excise taxes on alcohol (and possibly tobacco) as a means of dampening the growth of the personal income tax (PIT) component. In my opinion, a tax "mix" is not necessary. The natural growth of the personal income tax does not imply a bonus to the provinces, since the very *best* that the provinces can be expected to do is lower program growth to about 15 per cent, a rate not markedly different from the forecast for PIT. Moreover, it should be remembered that PIT growth is closely linked with cost growth, since both are propelled largely by wage and salary increases. Hence, full PIT growth would not only be a more realistic target than GNP growth, it would also be *fairer,* in that it implies a more equitable federal-provincial division of future risks.

The details we now have are enough to indicate that the federal proposal will just not work. In simple terms, it does not meet the provincial principles that Ontario and the other provinces have for so long enunciated.

THE REVENUE GUARANTEE AND EQUALIZATION

I have spoken at length on the principles that, as I perceive it, are of considerable importance to *all* provinces in assessing any new financing proposal. I myself feel that there is an additional principle to keep in mind. It is that **the federal government should receive no fiscal dividends from any actions relating to the Revenue Guarantee.**

The federal government is already in the process of "recapturing" some $900 million from the provinces through its unilateral and retroactive change in the Guarantee formula. Even more important is its recent advice that, for purposes of provincial budgetary planning, the Guarantee will be terminated after 1976. It is, of course, recognized that the Guarantee was originally intended for only five years. However, the difference between the old and new tax streams has turned out to be so large that a termination is now almost unthinkable. Provincial revenues would be seriously undermined, and the country's fiscal imbalance worsened. Is it fair that the relatively poorer level of government be saddled with the long-run costs of Tax Reform, while the relatively richer level reaps a bonus in perpetuity? Is it fair to force the provinces to raise taxes simply to restore their former revenue yield, thus leaving taxpayers across Canada with a higher total tax burden?

Ontario is on record as favouring a transfer of 4 personal income tax points to the provinces as a permanent replacement for the Revenue Guarantee. If this is not acceptable to the federal government, then I suggest that we turn to the comprehensive proposal recently made by my colleague from Quebec, the Honourable Raymond Garneau. His idea is that the "shadow" Revenue Guarantee payments beyond 1976 should be re-deployed to enrich both equalization and the fiscal equivalence for the three shared-cost programs. Ontario accepts this. As part of the solution to the shared-cost problem, *we are prepared to surrender our potential future Guarantee payments* provided that some of these savings to the federal government are turned back to the less wealthy provinces.

THE ONTARIO APPROACH

This brings me logically to the preferred Ontario approach. **Our preference is for "clean" opting out, with equalization to the level of the top province.** I believe that 20 personal income tax points transferred to the provinces would be a reasonable and fair exchange for complete federal withdrawal from Hospital Insurance, Medicare, and post-secondary education. The mechanics of the transfer are straightforward. The federal government would reduce its income tax rates across the board by 20 per cent; the provinces would then increase *their* income tax rates to take up this vacated tax room. And the taxpayers of Canada would be left in exactly the same total tax position, except that more of their income tax dollars would flow to the provinces and less to Ottawa.

Tax Rates:	Present	Proposed
federal	100.0	80.0
provincial	30.5	50.5
Total tax burden	130.5	130.5
Tax Shares:		
federal	76.6	61.3
provincial	23.4	38.7
total field	100.0	100.0

The advantage of clean opting out is that it reduces administrative problems at the same time that it increases provincial program flexibility. A further advantage of the Ontario solution is that equalizing to the top would achieve at a stroke the important federal objective of equal per capita contributions to all provinces.

There are several lingering reservations about opting out, and these need to be answered. The most common objection is that it would cost too much. This is argued on two grounds.

One ground is that the PIT grows so fast that it would result in fiscal dividends to the provinces over the long run. The Ontario response is, first, that the federal estimates of PIT revenue growth are too high. As we gather more data on the effects of indexation, I suspect we will find that the long-run revenue growth is even lower than the 14-17 per cent projected by federal officials. Second, we believe the most that can be realistically expected is that provinces constrain their program expenditure growth to the 15 per cent range; since this is in the neighbourhood of the growth we expect for the personal income tax, there would be no bonus over program costs. And third, even if there were small fiscal dividends in the *distant* future, these surely are justified according to the benefit-of-the-doubt principle that I mentioned earlier.

The other ground is that the federal government could not afford to equalize the new tax points up to the top province yield. This is not the case. The difference in 1976 between 20 points of income tax equalized to the national average and equalized to the top provinces is only $314 million. This is less than half the Revenue Guarantee entitlements calculated for that year! **This simple calculation shows that the higher standard — with greater equity all around — could be financed by the federal government simply living up to its long-standing pledge that the provinces would not have to bear the long-run cost of Tax Reform.**

1976-77	Additional Cost of 20 Pts. Equal to Top	Revenue Guarantee Sacrificed (PIT only)
	($ million)	($ million)
Nfld.	14.5	14.0
P.E.I.	3.1	3.1
N.S.	21.7	20.8
N.B.	17.9	17.7
Que.	162.3	153.3
Ont.	—	265.7
Man.	26.7	34.6
Sask.	24.3	28.1
Alta.	43.8	56.5
B.C.	—	69.2
TOTAL	314.3	663.0

A different objection to opting out is that it would seriously impinge upon the federal government's ability to conduct anti-cyclical stabilization policy. I disagree. After a transfer of 20 personal income tax points, the federal government would still occupy 61 per cent of the basic income tax field. This is ample room to implement discretionary tax measures of historical magnitude, since no swing has ever exceeded 7.5 per cent of revenues. In any event, across-the-board income tax changes are no longer regarded as a policy panacea for a diversified and open economy. Contemporary economic thinking leans toward more *selective* stabilization measures at the federal level, complemented by provincial fiscal policies to meet the economic conditions that vary markedly from region to region.

It has also been suggested that opting out would impair the federal government's ability to pay equalization and redistribute incomes. Since the Ontario proposal does not require the federal government to pay out any more than it is currently doing — indeed considerably less — there can be no such problem. The fact that there has been a change in the *form* of its contribution in no way limits the federal government's capacity to finance its own programs.

A fourth objection is that equalizing the tax transfer to the top province yield would "fracture" the equalization formula by introducing two different standards. Considering the various arbitrary elements already embodied in that complex program, I fail to see the importance of this charge.

Finally, I would like to reassure all Canadians that there would be no deterioration of national standards under the Ontario solution. Ontario, and I am sure all other provinces, would agree to maintain the four basic standards — comprehensiveness of scope, universal coverage, public administration, and portability — already built into the Medicare program. On this important matter, there is absolutely *no* difference between the solution we advocate and what the Prime Minister himself proposed on June 14.

SUMMATION

In an earlier part of my statement, I suggested that the federal offer has been progressively devalued as far as the tax points are concerned. Ontario's responses, on the other hand, have been made increasingly more attractive to the federal government and the other provinces. Let me review what we regard as major concessions.

First, we have assumed more than our fair share of future risks by agreeing to a first-year fiscal equivalence that barely covers program costs, and a growth rate that still looks difficult to attain.

Second, by reforming Hospital Insurance immediately, rather than in 1981, we are offering the federal government the certainty that it seeks. This will also generate significant savings to Ottawa, since federal "contributions" over the next four years would increase at the rate of growth of the PIT, not at the higher rate of actual costs.

Third, we have effectively foreclosed for at least five or ten years any sharing for the health programs that are not currently shared. Other provinces will be able to afford "catch-up" from their enriched equalization; we in Ontario will have to economize and rationalize as best we can within the replacement tax room.

Fourth, we have offered to abandon future Revenue Guarantee payments provided that new funds are transferred to those provinces who need them most.

The proposal that Ontario is making is fair to all governments concerned. It is fair to the federal government because it meets its objectives at a cost substantially below what a *full* settlement on the Revenue Guarantee would entail. It is fair to the less wealthy provinces because it provides them with greater assistance for catching up. And it is fair to Ontario:

- **it gives us greater flexibility in meeting our own priorities;**
- **it gives us greater certainty in the planning of our programs; and**
- **it reduces bureaucracy, and frees civil servants at both levels of government to do what they each do best.**

Most important it is fair to the taxpayers of Canada. It increases the accountability of governments to those who pay the bill, it allows for greater cost-efficiency in the future, **and it does not cost one extra dollar.**

TAX TRANSFERS UNDER ONTARIO'S 20 POINT PROPOSAL

1976-77	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Average or Total
Per Capita Value of one PIT Point ($)	4.20	3.80	5.30	4.80	6.90	9.10	6.50	6.40	7.90	9.10	7.80
Equalization to National Average ($)	3.60	4.00	2.50	3.00	0.90	—	1.30	1.40	—	—	
Additional Equalization to Highest Province Yield ($)	1.30	1.30	1.30	1.30	1.30	—	1.30	1.30	1.20	—	
Total	9.10	9.10	9.10	9.10	9.10	9.10	9.10	9.10	9.10	9.10	
Population (000's)	559	120	833	688	6,243	8,353	1,025	935	1,824	2,507	23,087
Value of 20 Points at Top Province Yield ($ Millions)	102	22	152	125	1,136	1,520	187	170	332	456	4,202

SAVINGS TO FEDERAL GOVERNMENT UNDER 20 POINT TAX TRANSFER

($ Millions)

1976-77	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.	Total
Federal Contributions, 3 program total (1)	94	19	149	114	1,313	1,506	182	160	333	396	4,266
PIT Revenue Guarantee	14	3	21	18	153	266	35	28	56	69	663
Total Federal Payments	108	22	170	132	1,466	1,772	217	188	389	465	4,929
Value of 20 Points Equalization to Top (2)	102	22	152	125	1,136	1,520	187	170	332	456	4,202
Savings to Federal Government	6	—	18	7	330	252	30	18	57	9	727

(1) Incorporates existing ceilings. Excludes 4.357 + 1 existing tax component for post-secondary education.

(2) From Appendix #1.

MECHANICS OF A 20 POINT TAX TRANSFER

	In Ontario (30.5% PIT Rate)		In A Province With A 38.5% PIT Rate	
	Present	Proposed	Present	Proposed
Tax Rates				
Federal	100.0	80.0	100.0	80.0
Provincial	30.5	50.5	38.5	58.5
Total Burden	130.5	130.5	138.5	138.5
Shown on Tax Form				
Provincial tax as % of federal tax	30.5	63.1	38.5	73.1
Tax Occupancy				
Federal	76.6	61.3	72.2	57.8
Provincial	23.4	38.7	27.8	42.2
Total Field	100.0	100.0	100.0	100.0

GROWTH IN ONTARIO'S PROGRAM COSTS

($ Millions)

	1970-71	1973-74	1976-77	Cumulative Increase
Hospital Insurance	794	1,088	1,925	142%
Medicare	436	561	844	94%
Post-Secondary Education	599	817	1,306	118%
Three Program Total	1,829	2,466	4,075	123%

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